

Press Release: New Independence Standard  
GAO PRESS STATEMENT  
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Today, David M. Walker, Comptroller General of the United States and head of the General Accounting Office (GAO), announced significant changes to the auditor independence requirements under Government Auditing Standards. These standards, which were first published in 1972 and are commonly referred to as the "Yellow Book" cover federal entities and those organizations receiving federal funds. Various laws require compliance with the Comptroller General's auditing standards in connection with audits of federal entities and funds. Furthermore, many states and local governments and other entities, both domestically and internationally, have voluntarily adopted these standards.

While the new standard deals with a range of auditor independence issues, the most significant change relates to the rules associated with nonaudit, or consulting services. Auditors have the capability of performing a range of services for their clients. However, in some circumstances it is not appropriate for them to perform both audit and certain nonaudit services for the same client. In these circumstances, the auditor and/or their client will have to make a choice as to which of these services they will provide.

The focus of the changes to the auditor independence standard is to better serve the public interest and to maintain a high degree of integrity, objectivity, and independence for audits of government entities. The standard includes a principle-based approach to addressing this issue supplemented with certain safeguards. The new independence standard for nonaudit services is based on two overarching principles:

--Auditors should not perform management functions or make management decisions; and

--Auditors should not audit their own work or provide non-audit services in situations where the amounts or services involved are significant/material to the subject matter of the audit.

For nonaudit services that do not violate the above principles, certain supplemental safeguards would have to be met. For example: (1) personnel who perform nonaudit services would be precluded from performing any related audit work, (2) the auditor's work could not be reduced beyond the level that would be appropriate if the nonaudit work was performed by another unrelated party; and (3) certain documentation and quality assurance requirements must be met.

The new standard includes an express prohibition regarding auditors providing certain bookkeeping/recordkeeping services, and limits payroll processing and certain other services, all of which are presently permitted under auditing standards of the American Institute of Certified Public Accountants (AICPA). At the same time, the standard recognizes that auditors can provide routine advice and answer technical questions without violating these two principles or having to comply with the supplemental safeguards. The standard also provides examples of how certain services would be treated under the new rules.

The revisions contained in the new standard have gone through an extensive deliberative process over the past 3 years, including extensive public comments and input from the Comptroller General's Advisory Council on Government Auditing Standards. The Council includes 20 experts in financial and performance auditing and reporting drawn from all levels of government,

academia, private enterprise, and public accounting, who advise the Comptroller General on Government Auditing Standards.

The GAO received extensive comments from the AICPA and individual members of the public accounting profession. Many of these comments related to activities by small CPA firms. Their concerns centered on the fact that the new standards for nonaudit services would be inconsistent with the current practices permitted under AICPA independence rules and could cause a hardship on the auditors and management of audited entities that receive nonaudit services. The views of all parties that formally commented on an exposure draft of the new standards were thoroughly considered by the Comptroller General in making this decision.

In the final analysis, protecting the public interest and ensuring public confidence in the independence of auditors of government financial statements, programs, and operations, both in form and substance, were the overriding considerations in the Comptroller General's decision to adopt these new standards for nonaudit services. According to Comptroller General David M. Walker, "This standard represents an important step to enhance the independence of external auditors and better protect the public. It is our hope that the AICPA will raise its independence standards to those contained in this new standard in order to eliminate any inconsistency between this standard and their current standards."

According to Comptroller General Walker, this new standard is the first of several planned steps in connection with nonaudit services covered by the Yellow Book. For example, the Comptroller General plans to work with the Federal Accounting Standards Advisory Board, which develops generally accepted accounting principles for the federal government, to determine what type of additional disclosures relating to nonaudit services may be appropriate. In addition, Comptroller General Walker has asked his Advisory Council on Government Auditing Standards to review and monitor this area to determine what, if any, additional steps may be appropriate.

In a separate but related matter, Comptroller General David M. Walker, Secretary of the Treasury Paul H. O'Neill, Office of Management and Budget Director Mitchell E. Daniels and Office of Personnel Management Director Kay Coles James, who comprise the Principals of the Joint Financial Management Improvement Program, have agreed that the 24 major departments and agencies covered by the Chief Financial Officers Act should have audit committees. The scope, structure and timing of this new requirement will be determined over the next several months. This will include determining what role these audit committees might play in connection with nonaudit services.

Because of the breadth of changes in the new standards, they are applicable to all audits for periods beginning on or after October 1, 2002. However, early implementation is encouraged.

The new audit standard is available on GAO's web site at <http://www.gao.gov/govaud/ybk01.htm> .